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SUBJECT: ZOMBIE FIRMS HAUNT IRAQ'S ECONOMY

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¶1. Summary: Many of Iraq's state-owned enterprises (SOEs) are economic zombies -- the GOI won't let them die, and they do not have the means to become viable on their own. At a chemical and sack plant in Babil Province, for instance, less than half the employees actually work, but the Ministry of Industry and Minerals (MIM) still funds the entire bloated payroll. Meanwhile, managers remain bound by MIM rules that increase costs, pushing the operation even further from profitability. While MIM is reportedly ready to finance new machinery, investment alone is not enough, for its main customers are other SOEs with uncertain futures. End summary.

Bird Watching at the Sack Factory

¶2. Jabbar Lool is the Director General of the Al Furatt Company (www.furattco.com) in Sadat al Hindiya, a town on the Euphrates about 50 miles south of Baghdad. Jabbar's company makes industrial chemicals, corn starch, and woven plastic sacks for fertilizer, grain and cement. About 600 of just over 2,000 Al Furatt employees work at the sack factory -- that is, they are paid to make sacks, but no more than 200 work on a typical day. While the theoretical production is 10 million sacks a year, the current output is just a fraction of that. On a tour of the sack factory on April 26, only about 50 workers were visible on the shop floor, where five of the seven production lines had been idle for years. In some corners of the factory, birds flitted between silent ranks of dilapidated machines.

¶3. Every sack Jabbar produces goes to the North Fertilizer Company, another SOE. That happens by order of the MIM, not the market. The sacks from Babil are 40-percent more expensive than the ones MIM imports from Syria. Jabbar reckons that labor accounts for about half of a sack's production cost. Based on other data Jabbar gave the PRT, total average cost is well over a dollar per sack. MIM pays Jabbar about 50 cents per sack.

A Faith-Based Business Plan

¶4. To be competitive, Jabbar must bring his costs down. That requires a multi-million dollar investment in modern equipment. Jabbar and his production managers think that with at least USD 12 million dollars for new machines, the factory can bring unit cost down to 48 cents and achieve an average annual rate of return just over 20 percent. MIM has reportedly promised several million for new equipment, and the Task Force to Improve Business Stability Operations is ready to chip in USD 1.5 million of equipment.

¶5. But that may not be enough to give the sack factory a future. Even with financing in hand, Jabbar may not procure his own equipment. That has to be arranged through MIM, a time-consuming process, and time is money for SOEs just as for any other business. And with factory workers technically designated as civil service employees, their life-time employment is guaranteed. These and other bureaucratic restrictions leave Jabbar with practically no means of effecting a turn-around.

¶6. MIM says subsidies for SOEs will end in 2011. The GOI's determination to follow through on that policy is open to question, but the prospect is nevertheless daunting for the Al Furratt Company. Jabbar's projections of profitability after a capital injection are based on the assumption that he can carry on selling sacks to other SOEs. But if other SOEs lose their subsidies too, Jabbar's business plan starts to look more like wishful thinking.

Comment

¶7. Al Furatt, like other SOEs (reftels) is an economic zombie -- the GOI will not let it die but it does not have the means to become viable on its own. Even with substantial injections of capital, SOEs remain massively overburdened with excessive employees making it difficult to project a glide-path to privatization. Some SOE managers have told us they hope to jettison up to two-thirds of their workers through golden parachute retirements in the next two to four years. Still, managers remain concerned that political exigencies may mean that for every worker gone, one steps in to take their place.

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